Change Is Afoot At Equus Total Return Fund Inc.

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Shareholder have authorized a withdrawal of election to be considered a BDC, what happens next could mean huge returns over the next 12 months.

Shareholders Approve Withdrawal Of BDC Election

Change is afoot at Equus Total Return Fund Inc. The question, what is going on with that BDC election has been answered. Shareholders, in a recent vote, have authorized the board to move forward with plans to withdraw the BDC election and begin the process of transforming the company into a new and more versatile fund. This move has been a long time coming, originating with the initial election to be considered a BDC and intention to merge with MVC Capital, and only the latest in a series of restructurings and reorganizations that have been occurring in the realm of closed end funds and Business Development Companies.

"Under the terms of the reorganization, Equus intends to pursue a merger or consolidation with MVC, or a subsidiary of MVC, or one or more of MVC's portfolio companies (the "Consolidation"). Absent Equus merging or consolidating with/into MVC, the current intention is for Equus to (i) consummate the Consolidation, (ii) terminate its election to be classified as a business development company under the 1940 Act, and (iii) be restructured as a publicly-traded operating company focused on the energy and/or financial services sector."

The original election for BDC, pursuant to the Investment Company Act of 1940, was part of an earlier plan to transform the company that has hit a stonewall. That plan included a merger/takeover by MVC Capital, a larger and more liquid BDC, and a share swap that has resulted in EQS owning roughly 2% of the company. Equus originally received 395,839 shares of MVC and has since received another 65,453 shares in the form of dividend distributions.

Under the terms of that agreement

EQS may have to repurchase its shares from MVC but there is no word yet on that front. MVC holds at minimum 2.112 million shares which, at the time of exchange, were trading around the same level they are today and worth a little more than $4 million. Equus holding's in MVC are only worth about $3.9 million, down roughly 33% from the time of exchange, and just about enough to cover the cost of buying its shares back, a wash in terms of portfolio value.

If Equus is able to consummate this new plan it would result in the formation of a new operating company and cease to be a closed-end fund. As an operating company Equus would no longer be subject to limitations and restrictions set forth by the 1940 ACT but still under the jurisdiction of the Securities Exchange Act, NYSE rules and Deleware corporate law. Among the many benefits are end to strict restrictions on leverage, the types of investments and ability of the company to change as needed. Other benefits include less restrictive share repurchase regulations, the ability to issue securities other than common stock and others that are expected to help unlock growth opportunities, enhance shareholder value and improve liquidity.

In order to complete the transformation Equus or one of it's subsidiaries will have to acquire or merge with a currently functional operating company or one of its subsidiaries within the time allotted by shareholders. The authorization is valid through the end of July, 2017 and that is where the risks lie. In order to complete the plan management has to come up with a definitive agreement to "Consolidate", that agreement must be approved by shareholders and then brought to fruition. If they are not able to

fulfill the terms in time the election for consideration as BDC may not be withdrawn.

What Is Equus Total Return Fund

The Equus Total Return Fund is a closed end fund with a rocky record. Originally formed in the '80's it has since suffered from ill timed investments and plunging oil prices that sent NAV to historic lows, and the discount to NAV even lower. While not a red-hot investment opportunity the fund is attractive on a valuation basis, and on the rebound from earlier woe. Non-performing assets include a media company and unpaid loans to two technology based start-ups. The attractive and positively peforming portion of the portfolio includes the holdings in MVC Capital, a substantial stake in the energy sector and an 18.7% stake in a company called Pallet One,

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Inc which together are the bulk of holdings.

Over the past year a number of positive developments have led to an increase in NAV and share prices. For one, the non-performing portions of the portfolio have stopped hemorrhaging value, some really bad investments may finally get written off. For another, energy prices have bottomed and begun to rise again, lifting the value of Equus energy holdings. Yet another is that investment in Pallet One, Inc, the most valuable portion of the portfolio, has begun to pay off in spades. Over the course of the past 6 quarters or so Pallet One, Inc has seen an increase in TTM revenues and earnings that have driven triple digit increases in the companies value.

- Over the course of the last 12 months the value of Pallet One has increased 275% from $5.6 million to $15.4 million. Pallet One, Inc. is one of North America's largest manufacturers of wooden shipping pallets and does business globally.

At last report NAV is $3.27, up 4.5% quarter to quarter and just over 10% year over year, which gives a discount of 38% at today's prices. This is much narrower than the 50% discount offered last year but still a substantial savings on the operational portion of the portfolio and the substantial cash position I have not yet mentioned. Along with positively performing assets valued at more than $24.5 million the company is also sitting on another $12 million in cash that helps round out the roughly $41.5 million in net assets.

Regardless the outcome of this latest twist to the EQS transformation saga it is clear that EQS is severely undervalued and being accumulated. Best case scenario the consolidation and change to operating company will unleash shareholder value in a number of ways. This could lead to an increase in NAV, a narrowing of the discount to NAV and perhaps even the reinstatement of dividend payments that could result in total returns of greater than 100% over the next 12 months. Each time the board and managing officers move forward with this plan will be a catalyst to attract new money, increase liquidity and further shrink today's massive discount. If they are not able to complete the consolidation, well then we're still left with an undervalued fund with growing NAV and a hoard of cash.